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SBA

The Business Plan for Homebased Business

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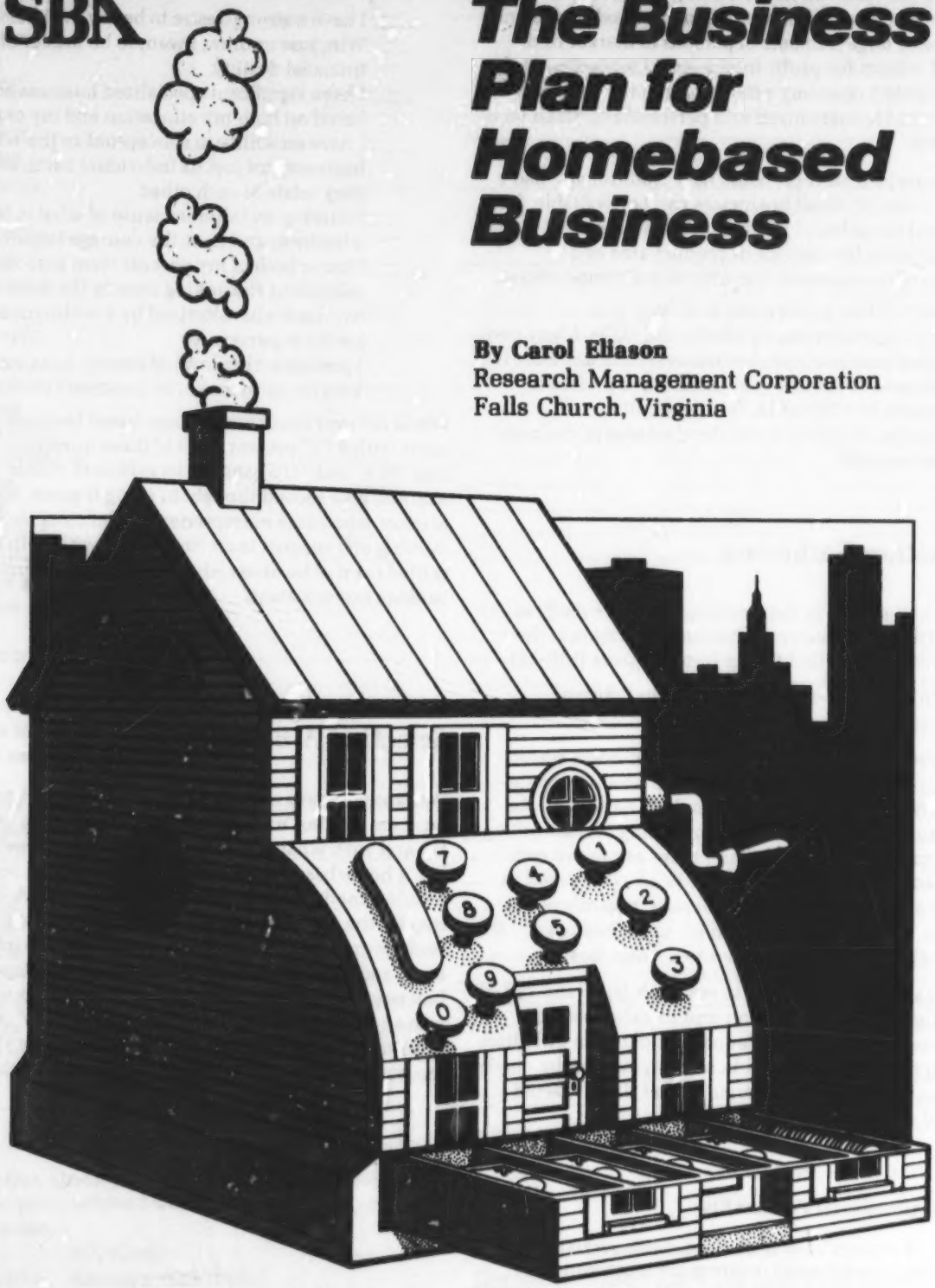

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Introduction

Homework has taken on new meaning for more than 10 million Americans. The drive for economic self-sufficiency has motivated large numbers of persons to market their skills and talents for profit from home. Our increasingly service oriented economy offers a widening spectrum of opportunities for customized and personalized small business growth.

Though untrained entrepreneurs have traditionally had a high rate of failure, small businesses can be profitable. Success in small home based business is not an accident. It requires both skills in a service or product area and acquisition of management and attitudinal competencies.

The purpose of this publication is to help you take stock of your interests, aptitudes and skills. Many people have good business ideas but not everyone has what it takes to succeed. If you are convinced that a profitable home business is attainable, this publication will provide step by step guidance in development of the basic written business plan.

Information Gathering

A helpful tool for use in determining if you are ready to take the risks of a home based business operation is the SBA publication entitled Going Into Business (MP–12).

It will help you focus on the basic steps in information gathering and business planning.

While the reasons for the rapid growth of home based business operations may vary from the need to supplement family income with a few hundred dollars all the way to a sophisticated technical consulting service billing hundreds of thousands of dollars, there are many common characteristics and challenges to be considered in launching most home based businesses, regardless of size. Some tasks are universal to all small business startups, while others are unique to a home base.

Careful planning, is required to research legal and tax issues, proper space utilization and to establish time management discipline. Inadequate or careless attention to development of a detailed business plan can be costly for you and your family in terms of lost time, wasted talent and disappearing dollars.

The Entrepreneurial Personality

A variety of experts have documented research that indicates that successful small business entrepreneurs, have some common characteristics. How do you measure up? On this checklist, write a "Y" if you believe the statement describes you; an "N" if it doesn't; and a "U" if you can't decide:

____ I have a strong desire to be my own boss.
____ Win, lose or draw, I want to be master of my own financial destiny.
____ I have significant specialized business ability based on both my education and my experience.
____ I have an ability to conceptualize the whole of a business; not just its individual parts, but how they relate to each other.
____ I develop an inherent sense of what is "right" for a business and have the courage to pursue it.
____ One or both of my parents were entrepreneurs; calculated risk-taking runs in the family.
____ My life is characterized by a willingness and capacity to persevere.
____ I possess a high level of energy, sustainable over long hours to make the business successful.

While not every successful home based business owner starts with a "Y" answer to all of these questions, three or four "N's" and "U's" should be sufficient reason for you to stop and give second thought to going it alone. Many proprietors who sense entrepreneurial deficiencies seek extra training and support their limitations with help from a skilled team of business advisors such as accountants, bankers and attorneys.

Selecting A Business

Perhaps you have already decided what your home based business will be. You know how you will serve your market and with what. If not, but you are determined to establish a home based source of income, then you need to decide exactly what business you will enter. A logical first step for the undecided is to list potential areas of personal background, special training, educational and job experience, and special interests that could be developed into a business. Review the following list of activities which have proven marketable for others. On a scale of "0" (no interest or strength) to 10 (maximum interest or strength) indicate the potential for you and a total score for each activity.

	My Level of Interest	Personal Strength	Market Strength	Total Points
Personal services				
— house cleaning				
— babysitting				
— tutoring				
— secretarial				
— catering				
— direct mail				
Handicrafts				
— needle work				
— ceramics				
— jewelry design				
— upholstering				
Artistic work				
— painting				
— photography				
— prints				
— wire sculpture				
— engraving				
Repair services				
— small appliances				
— furniture				
— clothing				
— TV and radio				
— automotive				
Instruction skills				
— languages				
— math				
— gourmet cooking				
— music				
— home repairs				
Mail order ideas				
— product sales				
— repairs				
— business service				
Seasonal products				
— foodstuffs				
— clothing				
— gift items				
Party sales				
— cookware				
— plants				
— plastic goods				
— cosmetics				
Your own ideas				

For other ideas, check your local public library for one or more of the publications listed in the Resource section of this publication.

SCORING

0 to 10	Almost a sure loser.
11 to 15	Reconsider but proceed with caution.
16 to 20	Some potential here, worth further study
21 to 25	Probably a winner, if you answered correctly.
26 to 30	How can you lose?

This checklist should give you a good idea of the kind of business that would suit you best and why.

Time Management

For both the novice and the experienced business person planning a small home based enterprise, an early concern requiring self-evaluation is time management.

It is very difficult for some people to make and keep work schedules even in a disciplined office setting. At home, as your own boss, the problem can be much greater. To determine how much time you can devote to your business, begin by drafting a weekly task timetable listing all current and potential responsibilities and the blocks of time required for each. When and how can business responsibilities be added without undue physical or mental stress on you and your family? Potential conflicts must be faced and resolved at the outset and as they occur, otherwise your business can become a nightmare. During the first year of operation, continue to chart, post and checkoff tasks on a daily, weekly and monthly basis.

Distractions and excuses for procrastination abound. It is important to keep both a planning and an operating log. These tools will help avoid oversights and provide vital information when memory fails.

To improve the quality of home work time, consider installation of a separate telephone line for the business and attach an answering machine to take messages when you do not wish to be distracted or are away from home. A business line has the added advantage of allowing you to have a business listing in the phone book and, if you wish to buy it, an ad in the classified directory.

Is A Home Based Business Site Workable?

- Where in the home will the business be located?
- What adjustments to living arrangements will be required?
- What will be the cost of changes?
- How will your family react?
- What will the neighbors think?

It will be important to set aside a specific work area. For example, more than one fledgling business ledger has gone up in smoke, been chewed by the family dog, or thrown out with the trash when business records were not kept separate from family papers. Ready access to business records during work hours is essential, but they must be protected.

Check the reasons below for and against working at home that apply to you. List any additional drawbacks or obstacles to operating this business at home.

Pros	Cons
Lower startup costs	Isolation
Lower fixed costs	Space limitations
Tax benefits	Zoning
Lifestyle flexibility	Security concerns
No commuting	Household interference

Note that changes in personal habits will be required. Examples:

- Self discipline to keep TV off while working.
- Limiting personal telephone calls in length and number.
- Diligence in meeting work deadlines when no one is checking.

Ask family members to comment on pros and cons. Their concerns may require reconsideration of some specifics.

Is A Home Based Business Site Allowable?

Now you will want to investigate potential legal and community problems associated with operating the business from home. You should gather, read and digest specialized information concerning federal, state, county and municipal laws and regulations concerning home based business operations.

Check first! Get the facts in writing. Keep a topical file for future reference. Some facts and forms will be needed for your business plan. There may be limitations enforced that can make your planned business impossible or require expensive modifications to your property.

Items to be investigated, recorded and studied are:

TO DO	DONE	
_____	_____	county or city zoning code restrictions
_____	_____	necessary permits and licenses for operation
_____	_____	state and local laws and codes regarding zoning
_____	_____	deed or lease restrictions such as covenants and restrictive conditions of purchase
_____	_____	parking and customer access; deliveries
_____	_____	sanitation, traffic and noise codes
_____	_____	signs and advertising
_____	_____	state and federal code requirements for space, ventilation, heat and light
_____	_____	limitations on the number and types of workers. If not, check with the local Chamber of Commerce office
_____	_____	reservations that neighbors may have about a business next to or near them

Here are some ways to collect your information. Call or visit the zoning office at county headquarters or city hall. In some localities the city or county Office of Economic Development has print materials available to pinpoint key "code" items affecting home based business.

Even in rural areas, the era of unlimited free enterprise is over. Although the decision makers may be in the state capital or in a distant regional office of a federal agency, check before investing in inventory, equipment or marketing programs. If in doubt call the state office of Industrial Development or the nearest SBA district office. In some states the county agent or home demonstration agent will have helpful information concerning rural or farm business development.

To cover the income tax rules regarding a home based business, be sure to secure the IRS Publication #587, *BUSINESS USE OF YOUR HOME.*

Is The Home Based Business Site Insurable?

In addition to community investigations, contact your insurance company or agent. It is almost certain that significant changes will be required in your coverage and limits when you start a home based business. When you have written a good description of your business, call your agent for help in insuring you properly against new hazards resulting from your business operations such as:

- fire, theft and casualty damage to inventories and equipment
- business interruption coverage
- fidelity bonds for employees
- liability for customers, vendors and others visiting the business
- workmen's compensation
- group health and life insurance
- product liability coverage if you make or sell a product; workmanship liability for services
- business use of vehicle coverage

Overall Home Site Evaluation

After you have gathered as much information as seems practical you may wish to evaluate a home based site vs. one or more other nearby locations. Here's a handy checklist. Using the "0" to "10" scale, grade these vital factors:

Factors To Consider

	Grades For Each Factor	
	Home	**Other**
1. Customer convenience	_____	_____
2. Availability of merchandise or raw materials	_____	_____
3. Nearby competition	_____	_____
4. Transportation availability and rates	_____	_____
5. Quality and quantity of employees available	_____	_____
6. Availability of parking facilities	_____	_____
7. Adequacy of utilities (sewer, water, power, gas)	_____	_____
8. Traffic flow	_____	_____
9. Tax burden	_____	_____
10. Quality of police and fire services	_____	_____
11. Environmental factors	_____	_____
12. Physical suitability of building	_____	_____
13. Provision for future expansion	_____	_____
14. Vendor delivery access	_____	_____
15. Personal convenience	_____	_____
16. Cost of operation	_____	_____
17. Other factors including how big can you get without moving	_____	_____
Totals	_____	_____

The greater the difference between the totals of the two columns, the clearer your decision should be. In the space

below, write out your decision and the reasons that support it.

Decision:_____

_____

_____

_____

_____

Writing The Business Plan

Now that your research and plan development is nearing completion, it is time to move into action. If you are still in favor of going ahead, it is time to take several specific steps. The key one is to organize your dream scheme into a business plan.

What is it?

- A business plan is written by the home based business owner with outside help as needed
- It is accurate and concise as a result of careful study
- It explains how the business will function in the marketplace
- It clearly depicts its operational characteristics
- It details how it will be financed
- It outlines how it will be managed
- It is the management and financial "blueprint" for startup and profitable operation
- It serves as a prospectus for potential investors and lenders

Why create it?

- The process of putting the business plan together, including the thought that you put in before writing it, forces you to take an objective , critical, unemotional look at your entire business proposal
- The finished written plan is an operational tool which, when properly used, will help you manage your business and work toward its success
- The completed business plan is a means for communicating your ideas to others and provides the basis for financing your business

Who should write it?

- The home based owner to the extent possible
- Seek assistance in weak areas, such as:
  - accounting
  - insurance
  - capital requirements
  - operational forecasting
  - tax and legal requirements

When should a Business Plan be used?

- To make crucial startup decisions
- To reassure lenders or backers
- To measure operational progress
- To test planning assumptions
- As a basis for adjusting forecasts
- To anticipate ongoing capital and cash requirements
- As the benchmark for good operational management

Proposed Outline For Home Based Business Plan

This outline is suggested for a small proprietorship or family business. Shape it to fit your unique needs. For more complex manufacturing or franchise operations see the Resource section for other options.

Part I. — Business Organization

Cover Page:

A. Business Name:

_____

Street Address:

_____

Mailing Address

_____

Telephone number:

_____

Owner(s) Name(s):

_____

Inside Pages:

B. Business Form:

_____

(proprietorship, partnership, corporation)
If incorporated

_____

(state of incorporation)

Include copies of key subsidiary documents in an appendix. Remember even partnerships require written agreements of terms and conditions to avoid later conflicts and to establish legal entities and equities. Corporations require charters, articles of incorporation and by-laws.

Part II. — Business Purpose and Function

In this section, write an accurate yet, concise description of the business. Describe the business you plan to start in narrative form.

What is the principal activity? Be specific. Give product or service description(s):

- retail sales?
- manufacturing?
- service?
- other?

How will it be started?

- a new startup
- the expansion of an existing business
- purchase of a going business
- a franchise operation
- actual or projected start up date

Why will it succeed? Promote your idea!

- how and why this business will be successful.
- what is unique about your business
- what is its market "niche"

What is your experience in this business? If you have a current resume of your career, include it in an appendix and reference it here. Otherwise write a narrative here and include a resume in the finished product. If you lack specific experience, detail how you plan to gain it, such as training, apprenticeship or working with partners who have experience.

_____
_____
_____
_____
_____
_____
_____
_____
_____
_____
_____
_____
_____
_____

The Marketing Plan

The marketing plan is the core of your business rationale. To develop a consistent sales growth a home based business person must become knowledgeable about the market. To demonstrate your understanding, this section of the home based business plan should seek to concisely answer several basic questions:

Who is your market?

- Describe the profile of your typical customer
  Age_____
  Male, female, both_____
  How many in family_____
  Annual Family Income_____
  Location_____
  Buying patterns_____
  Reason to buy from you_____
  Other_____
  _____
- Geographically describe your trading area (i.e., county, state, national)
  _____
  _____
- Economically describe your trading area: (single family, average earnings, number of children)
  _____
  _____

How large is the market?

- Total units or dollars _____
- Growing____ Steady____ Decreasing____
- If growing, annual growth rate_____

Who is your competition? No small business operates in a vacuum. Get to know and respect the competition. Target your marketing plans. Identify direct competitors (both in terms of geography and product lines), and those who are similar or marginally comparative. Begin by listing names, addresses and products or services. Detail briefly but concisely the following information concerning each of your competitors:

- Who are the nearest ones?
- How are their businesses similar or competitive to yours?
- Do you have a unique "niche"? Describe it.
- How will your service or product be better or more saleable than your competitors?
- Are their businesses growing? Stable? Declining? Why?
- What can be learned from observing their operations or talking to their present or former clients?
- Will you have competitive advantages or disadvantages by operating from home? Be honest!

Remember, your business can become more profitable by adopting the good competitive practices and by avoiding their errors.

To help you evaluate how successful your product or service will be, go down the following list of standard characteristics (you may want to add more from your knowledge of your field) and make a candid evaluation of your com-

petitive "edge." On a scale of "0" (theirs puts mine to shame) to 10 (mine puts their to shame) indicate the potential for you and a total score:

FEATURE	
Price	____
Performance	____
Durability	____
Versatility	____
Speed/accuracy	____
Ease of operation or use	____
Ease of maintenance or repair	____
Ease or cost of installation	____
Size or weight or color	____
Appearance or styling or packaging	____
Total Points	____

A Total Points score of less than 60 indicates that you might reconsider the viability of your product or service or think about how you can improve it. Over 80 points indicates a clear competitive edge.

What percent of the market will you penetrate?

1. estimate the market in total units or dollars

_____

2. estimate your planned volume

_____

3. amount your volume will add to total market

_____

4. subtract 3 from 2

_____

Line 4 represents the amount of your planned volume that must be taken away from the competition.

What pricing and sales terms are you planning? The primary consideration in pricing a product or service is the value that it represents to the customer. If, on the previous checklist of features, your product is truly ahead of the field, you can command a premium price. On the other hand, if it is a "me too" product, you may have to "buy" a share of the market to get your foothold and then try to move price up later. This is always risky and difficult. One rule will always hold: ultimately, the market will set the price. If your selling price does not exceed your costs and expenses by the margin necessary to keep your business healthy, you will fail. Know your competitors pricing policies. Send a friend to comparison shop. Is there discounting? Special sales? Price leaders? Make some "blind" phone calls. Detail your pricing policy:

_____

_____

_____

What is your sales plan? Describe how you will sell, distribute or service what you sell? Be specific. Below are outlined some common practices:

Direct sales by telephone or in person. The tremendous growth of individual sales representatives who sell by party bookings, door to door, and through distribution of call back promotional campaigns suggests that careful research is required to be profitable.

Mail Order

Specialized markets for leisure time or unique products have grown as more two income families find less time to shop. Be aware of recent mail order legislation and regulation.

Franchising

a. You may decide to either buy into someone else's franchise as a franchisee or

b. Create your own franchise operation that sells rights to specific territories or product lines to others. Each will require further legal, financial and marketing research.

An excellent starting point if you are considering franchise involvement is the SBA publication **Evaluating Franchising Opportunities MP–26.** The International Franchise Association also publishes a number of valuable aids in this field.

Distributors

You may decide to work as a local or regional distributor for several different product lines.

Outline your sales plan below:

_____

_____

_____

What is your advertising plan? Each product or service will need its own advertising strategy as part of the total business marketing plan. Before developing an advertising campaign for your business plan, take time to review a few basic assumptions. By definition, advertising is any form of paid, non-personal promotion that communicates with a large number of potential customers at the same time. The purpose of advertising is to inform, persuade and remind customers about your company's products or services. Every advertising activity should have specific goals. Common examples are:

- To bring in sales orders or contracts
- To promote special events such as sales, business openings, new products
- To bring in requests for estimates or for a sales representative to call
- A special goal at the outset may be to use special me-

dia to establish yourself even before startup and to get potential customer "feedback."

These might include one or more of the following:

- Purchase and distribution of business cards to potential clients
- Posting notices on free bulletin boards in area supermarkets or office complexes
- A telephone survey of potential clients to alert them to your startup plans.

To assist in determining what types of advertising are appropriate and within company budget projections, it will be necessary to carefully review your customer profile. From this review, establish a clear statement of advertising goals. Write down what you want your advertising to accomplish:

_____
_____
_____
_____

The next step will be to develop answers to the following crucial questions:

Q. What should be said about the business and how should it be stated?

A. _____
_____

Q. What media should be used?

A. _____
_____

Q. How much can be afforded?

A. _____
_____

Q. How can the advertising program be implemented?

A. _____
_____

Q. How can its effectiveness be measured?

A. _____
_____

The basic criteria for selecting specific types of media will include concise answers to the following:

- **Trading Area** — Do you plan to serve or sell to an industrial market, a national market, a neighborhood or specialized market? Describe yours: _____
_____

- **Customer Type** — What does your potential customer read or listen to? Where? How often? What image does the media you are considering suggest? Does it fit your customer? Describe your customer: _____
_____

- **Budget Restrictions** — How will the amount of money you have to spend limit the media you can use? How can you spread your budget out over a year to give a repetitive, continuous message? While you may have to spend more at the start, a good ongoing guideleine is that advertising should not exceed one or two percent of sales. Set forth how much you are willing to invest in advertising in the first year:
  $_____
  Break into months or quarters:
  $_____ $_____ $_____ $_____ $_____ $_____
  $_____ $_____ $_____ $_____ $_____ $_____

- **Continuity of Message** — How will the type of product or service, customer profile and seasonal buying patterns affect your choice of media and the frequency with which you advertise? Explain your message here: _____
_____
_____

- **Past Performance** — What is the track record for use of the medium you are considering for your type of business? What do your competitors use? What does your trade association suggest? Enter appropriate comments here: _____
_____

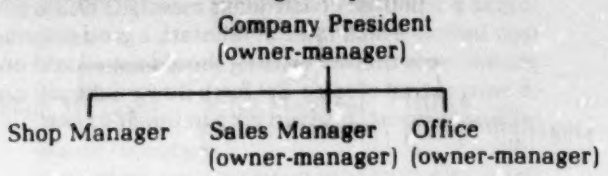
Management Plan

Who will do what? Be sure to include four basic sets of information:

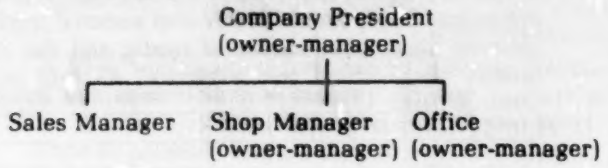
1. State a personal history of principals and related work, hobby or volunteer experience (include formal resumes in Appendix)
2. List and describe specific duties and responsibilities of each
3. List benefits and other forms of compensation for each
4. Identify other professional resources available to the business: Example: Accountant, lawyer, insurance broker, banker. Describe relationship of each to business: Example: "accountant available on part time hourly basis, as needed, initial agreement calls for services not to exceed x hours per month at $xx.xx per hour."

To make this section graphically clear, start with a simple organizational chart that lists specific tasks and shows, who (type of person is more important than individual name

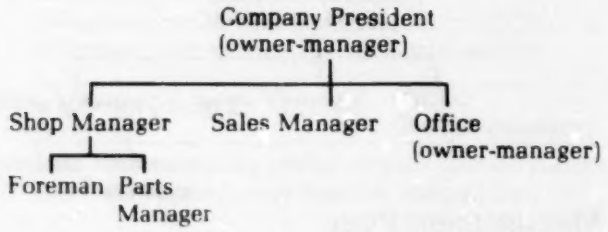
other than for principals) will do *what* indicated by arrows, work flow and lines of responsibility and/or communications. Consider the following examples:



or like this?



As the service business grows, its organization chart could look like this:



Concisely answer the following questions.

Q. What are your personnel needs now?

A. 1._____
2._____
3._____
4._____

Q. What skills must each key person have?

A. 1._____
2._____
3._____
4._____

Q. Are the people needed available? Name them, indicate full or part time and salary rates:

A. 1._____
2._____
3._____
4._____

Detail a proposed work schedule by week and month for at least the first year.

Calculate total salaries, wages, fringe benefits and payroll taxes for each month of the first year:

	Compensation	Fringe Benefits	Payroll Taxes
1st Mo.	$_____	$_____	$_____
2nd Mo.	$_____	$_____	$_____
3rd Mo.	$_____	$_____	$_____
4th Mo.	$_____	$_____	$_____
5th Mo.	$_____	$_____	$_____
6th Mo.	$_____	$_____	$_____
7th Mo.	$_____	$_____	$_____
8th Mo.	$_____	$_____	$_____
9th Mo.	$_____	$_____	$_____
10th Mo.	$_____	$_____	$_____
11th Mo.	$_____	$_____	$_____
12th Mo.	$_____	$_____	$_____
Full Yr.	$_____	$_____	$_____

If you have identified any gaps in personnel skills, state how these will be overcome by training, purchase of outside services or subcontracting. Check with the nearest state employment service office for assistance. Write your plan:

_____
_____
_____
_____

What is your banking plan?

What will be the location and type of bank accounts opened for the business. A word of caution, keep business accounts separate from personal or family accounts. These vital records will be necessary for future tax and accounting purposes. Describe your banking plan:_____
_____
_____
_____

How Is Your Credit Rating?

There may be several partial answers to this question. All will be of importance to the future of the business. First, what is your personal history of paying debts? Just to be safe, purchase a copy of your personal credit record from the local credit bureau for a small fee and make sure that it is accurate. Look in the classified telephone directory under "Credit Reporting Agencies."

To establish a credit rating, it is necessary to secure credit with a number of businesses and to use it. Your rating will be based upon your record for paying for goods and services based upon the agreed terms. If your prior credit rating is poor, discuss with your lawyer, accountant and banker options for improvement before seeking and being refused business credit.

Operational Plans Summary

The purpose of this section is to summarize from previous sections, the various operations of your business and link them to the finance section of your business plan. In addition you will want to summarize the advantages and disadvantages of a home based business operation. Refer to your earlier checklist. Write your summary here:

_____
_____
_____
_____
_____
_____
_____
_____
_____
_____
_____

The Financial Plan

Clearly the most critical section of your Business Plan Document is the Financial Plan. In formulating this part of the planning document, you will establish vital schedules that will guide the financial health of your business through the troubled waters of the first year and beyond.

Before going into the details of building the Financial Plan, it is important to realize that some basic knowledge of accounting is essential to the productive management of your business. If you are like most home business owners, you probably have a deep and abiding interest in the product or services that you sell or intend to sell. You like to do what you do, and it is even more fulfilling that you are making money doing it. There is nothing wrong with that. Your conviction that what you are doing or making is worthwhile is vitally important to success. Nonetheless, the income of a coach who takes the greatest pride in producing a winning team will largely depend on someone keeping score of the wins and losses.

The business owner is no different. Your product or service may improve the condition of mankind for generations to come, but, unless you have access to an unlimited bankroll, you will fail if you don't make a profit. If you don't know what's going on in your business, you are not in a very good position to assure its profitability.

Most home based businesses will use the "cash" method of accounting with a system of recordkeeping that may be little more than a carefully annotated checkbook in which is recorded all receipts and all expenditures, backed up by a few forms of original entry (invoices, receipts, cash tickets). For a Sole Proprietorship, the business form assumed by this Management Aid, the very minimum of recorded information is that required to accurately complete the federal Internal Revenue Service Form 1040, Schedule C. Other business types (partnerships, joint ventures, corporations) have similar requirements but use different tax forms.

If your business is, or will be, larger than just a small supplement to family income, you will need a something more sophisticated. Stationery stores can provide you with several packaged small business accounting systems complete with simple journals and ledgers and detailed instructions in understandable language.

Should you feel that your accounting knowledge is so rudimentary that you will need professional assistance to establish your accounting system, the classified section of your telephone directory can lead you to a number of small business services that offer a complete range of accounting services. You can buy as much as you need, from a simple "peg-board" system all the way to computerized accounting, tax return service and monthly profitably consultation. Rates are reasonable for the services rendered and an investigative consultation will usually be free. Look under the heading, "Business Consultants," and make some calls. Be sure to let them know the size of your business so you get to the ones who specialize in home based operations. Many of them are home-based entrepreneurs themselves, and know what you will be going through.

Let's start by looking at the makeup of the Financial Plan for the business.

The Financial Plan includes the following:

1. **Financial Planning Assumptions** — these are short statements of the conditions under which you plan to operate.
   - Market health _____
   - Date of startup _____
   - Sales buildup ($) _____
   - Gross profit margin _____
   - Equipment, furniture and fixtures required _____
   - Payroll and other key expenses that will impact the financial plan _____
2. **Operational Plan — Profit and Loss Projection** — this is prepared for the first year, broken into twelve individual months. It should become your first year's Budget. See Exhibits A & A-1.
3. **Source of Funds Schedule** — this shows the source(s) of your funds to capitalize the business and how they will be distributed among your fixed assets and working capital.
4. **Pro Forma Balance Sheet** — "Pro forma" refers to

the fact that the balance sheet is before the fact, not actual. This form displays Assets, Liabilities and Equity of the business. This will indicate how much Investment will be required by the business and how much of it will be used as Working Capital in its operation.

5. **Cash Flow Projection** — this will forecast the flow of cash into and out of your business through the year. It helps you plan for staged purchasing, high volume months and slow periods.

Creating the Profit and Loss Projection

Refer to Exhibits A & A-1. Create a wide sheet of analysis paper with a three inch wide column at the extreme left and thirteen narrow columns across the page. Write at the top of the first page the planned name of your business. On the second line of the heading, write "Profit and Loss Projection." On the third line, write "First Year."

Then, note the headings on Exhibit A and copy them onto your 13-column sheet. If startup is indefinite, just write "Month #1", Month #2", etc. Column 13 should be headed "Total Year."

In the wide, unnumbered column on the left of your 13-column sheet, copy the headings from the similar area on Exhibit A. Then follow the example set by Exhibit A and list all of the other components of your income, cost and expense structure. You may add or delete specific lines of expense to suit your business plan. Guard against consolidating too many types of expense under one account lest you lose control of the components. At the same time, don't try to break down expenses so discretely that accounting becomes a nuisance instead of a management tool. Once again, Exhibit A provides ample detail for most home based businesses.

Now, in the small column just to the left of the first monthly column, you will want to note which of the items in the left-hand column are to be estimated on a monthly (M) or a yearly (Y) basis. Items such as Sales, Cost of Sales and Variable Expenses will be estimated monthly based on planned volume and seasonal or other estimated fluctuations. Fixed Expenses can usually be estimated on an yearly basis and divided by twelve to arrive at even monthly values. The "M" and "Y" designations will be used later to distinguish between variable and fixed expense.

Depreciation allowances for Fixed Assets such as production equipment, office furniture and machines, vehicles, etc. will be calculated from the Source of Funds Schedule.

Exhibit A-1 describes line by line how the values on the Profit and Loss Projection are developed. Use this as your guide.

Source of Funds Schedule

To create this schedule, you will need to create a list of all of the Assets that you intend to use in your business, how much investment each will require and the source of funds to capitalize them. A sample of such a list is shown below:

ASSET	COST	SOURCE OF FUNDS
Cash	$ 2,500	Personal savings
Accounts Receivable	3,000	From profits
Inventory	2,000	Vendor Credit
Pickup truck	5,000	Currently owned
Packaging machine	10,000	Installment purchase
Office desk and chair	300	Currently owned
Calculator	75	Personal cash
Electric Typewriter*	500	Personal savings

*A note about office equipment: although this Management Aid has been written for a broad audience of home based business operators, those who plan enterprises which produce printed products or a large volume of correspondence should consider an electronic word processor as a great time saver. Test use or rent two or more brands that appear to meet your needs and select the one with which you feel most comfortable. Don't be afraid to ask others who have had to make this decision for advice. Compatability of your system with those of potential typesetting services or printers should be of high consideration. If you are not quite sure, consider renting or leasing the equipment until you are. Service contracts on such complex electronic gear are usually a good insurance policy.

Before you leave your Source of Funds Schedule, indicate the number of months (years x 12) of useful life for depreciable fixed assets. (In the example, the pickup truck, the packaging machine and the furniture and office equipment would be depreciable.) Generally, any individual item of equipment, furniture, fixtures, vehicles, etc., costing over $100 should be depreciated. For more information on allowances for depreciation, you can get free publications and assistance from your local Internal Revenue Service office. Divide the cost of each fixed asset item by the number of months over which it will be depreciated. You will need this data to enter as monthly depreciation on your Profit and Loss Projection. All of the data on the Source of Funds Schedule will be needed to create the Balance Sheet.

Creating the Pro Forma Balance Sheet

Refer to Exhibit B. This is a Balance Sheet form. There are a number of variations of this form and you may find it prudent to ask your banker for the form that the bank uses for small business. It will make it easier for them to evaluate the health of your business. Use Exhibit B to get started and transfer the data to your preferred form later. Accompanying Exhibit B is Exhibit B-1 which describes line by line how to develop the Balance Sheet.

Even though you may plan to stage the purchase of some assets through the year, for the purposes of this pro forma Balance Sheet, assume that all assets will be provided at the startup.

Cash Flow Projection

An important subsidiary schedule to your financial plan is a monthly Cash Flow Projection. Prudent business management practice is to keep no more cash in the business than is needed to operate it and to protect it from catastrophe. In most small businesses, the problem is rarely one of having too much cash. A Cash Flow Projection is made to advise management of the amount of cash that is going to be absorbed by the operation of the business and compares it against the amount that will be available.

SBA has created an excellent form for this purpose and it is shown as Exhibit C. Your projection should be prepared on 13-column analysis paper to allow for a twelve month projection. Exhibit C-1 represents a line by line description and explanation of the components of the Cash Flow Projection which provides a step-by-step method of preparation.

A Final Word

In completing this publication, you have put in a great deal of time and effort. You should now have all of the elements needed to present as simple or sophisticated a prospectus for your enterprise as you desire. More important, you have created the management tools to guide you in your venture. Once the business opens its doors, you will be inundated by the details, problems, challenges and joys of going it alone. It will be difficult to hold to your course through the rough seas ahead, but don't forget this "chartbook", it will see you through to "Port Profit." It should be a living document, referred to regularly and often revised to reflect your experience. Begin a planning cycle that expands this first year plan into one that spans three or five years out. Update it at regular intervals. Set your goals and live by them. Your success is in your hands. Good planning and good execution!

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EXHIBIT A

OPERATING PLAN FORECAST (Profit and Loss Projection)

		Month 1			Month 2–12			Totals			
Revenue (sales)	Ind %	Estimate	Actual	%	Estimate	Actual	%	Estimate	%	Actual	%
Total Revenue (sales)											
Cost of Sales											
Total Cost of Sales											
Gross Profit											
Expenses											
Salary expense: Sales people, office and other											
Payroll Expenses (taxes, etc.)											
Outside Services											
Supplies (office and operating)											
Repairs and Maintenance											
Advertising											
Car, Delivery and Travel											
Accounting and Legal											
Rent											
Telephone											
Utilities											
Insurance											
Taxes (real estate, etc)											
Interest											
Depreciation											
Other Expenses (specify each)											
Miscellaneous (unspecified)											
Total Expenses											
Net Profit											

EXHIBIT A1

PROFIT AND LOSS PROJECTION

The profit and loss statement (P&L) is valuable as a planning tool and as a key management tool to help control operations to reach business goals. It enables the owner/manager to develop a "preview" of the amount of profit, or loss, generated each month, and for the business year — based on reasonable predictions of monthly levels of sales, costs, and expenses. The owner/manager can compare the year's expected profits or losses against the profit goals and needs established for the business. A completed P&L statement allows the owner/manager to compare actual figures with the monthly projections, and to take steps to correct any problems.

REVENUE (Sales)

- List the departments within the business, e.g., assume your business is appliance sales and service: New appliances, used ones, parts, in-shop service, on-site service.
- In the "Estimate" columns, enter a reasonable projection of monthly sales for each department of the business. Include cash and on-account sales. In the "Actual" columns, enter the actual sales for the month as they become available.
- Exclude from the Revenue section any revenue that is not strictly related to the business.

COST OF SALES

- Cite costs by department of the business, as above.
- In the "Estimate" columns enter the cost of sales estimated for each month for each department. For product inventory, calculate the cost of the goods sold for each department (beginning inventory plus purchases and transportation costs during the month, minus the inventory). Enter "Actual" costs when known each month.

Gross Profits — Subtract the total cost of sales from the total revenue.

EXPENSES

- *Salary Expenses:* Base pay plus overtime.
- *Payroll Expenses:* Include paid vacations, sick leave, health insurance, unemployment insurance, social security taxes.
- *Outside Services:* Include costs of subcontracts, overflow work farmed out, special or one-time services.
- *Supplies:* Services and items purchased for use in the business, not for resale.
- *Repairs and Maintenance:* Regular maintenance and repair, including periodic large expenditures such as painting or decorating.
- *Advertising:* Include desired sales volume, and yellow pages expenses, e.g.
- *Car, Delivery and Travel:* Include charges if personal car used in business, including parking, tolls, buying trips, etc.
- *Accounting and Legal:* Outside professional services.
- *Rent:* List only real estate used in the business.
- *Telephone:* Self-explanatory.
- *Utilities:* Water, heat, light, etc.
- *Insurance:* Fire or liability on property or products, workmen's compensation.
- *Taxes* (real estate, etc.): Inventory, sales, excise tax, others.
- *Interest:* Self-explanatory.
- *Depreciation:* Amortization of capital assets.
- *Other Expenses* (specify each): e.g., tools, leased equipment.
- *Miscellaneous* (unspecified): Small expenditures without separate accounts.

Net Profit — To find net profit, subtract total expenses from gross profit.

EXHIBIT B

Company Name

① **BALANCE SHEET**

As of (current date)

② **ASSETS**		**LIABILITIES**	⑦
Current Assets		**Current Liabilities**	
Cash	$_____	Accounts payable	$_____
Accounts receivable $_____		Short-term notes	$_____
less allowance for		Current portion	
doubtful accounts $_____		of long-term notes	$_____
Net realizable value	$_____	Interest payable	$_____
Inventory	$_____	Taxes payable	$_____
Temporary investments	$_____	Accrued payroll	$_____
Prepaid expenses	$_____	Total Current Liabilities	$_____ ⑧
③ Total Current Assets	$_____	**Long-Term Liabilities**	
Long-Term Investments		Notes payable	$_____
(detailed list)	$_____	Total Long-Term Liabilities	$_____ ⑨
④ Total Investments	$_____	**TOTAL LIABILITIES**	$_____ ⑦
Fixed Assets		**EQUITY**	
Land	$_____	Total Owner's Equity	
Buildings: $_____ at		(proprietorship)	$_____
cost, less accumulated		or	
depreciation of $_____		(Name's) Equity	$_____
Net book value	$_____	(Name's) Equity	$_____
Equipment: $_____ at		(partnership)	
cost, less accumulated		Total Partners' Equity	$_____ ⑩
depreciation of $_____		or	
Net book value	$_____	Shareholders' Equity	
Furniture/Fixtures: $_____ at		(corporation)	
cost, less accumulated		Capital stock	$_____
depreciation of $_____		Capital paid-in in excess	
Net book value	$_____	of par	$_____
Autos/Trucks: $_____ at		Retained earnings	$_____
cost, less accumulated		Total Shareholders' Equity	$_____
depreciation of $_____		**TOTAL LIABILITIES**	
Net book value	$_____	**AND EQUITY**	$_____ ⑪
⑤ Total Net Fixed Assets	$_____	**RECONCILEMENT OF EQUITY**	
Other Assets		**As of (current date)**	
(detailed list)	$_____	Equity at beginning of period	$_____
⑥ Total Other Assets	$_____	Plus: Net income (or Minus: Net	
② **TOTAL ASSETS**	$_____	loss) after taxes	$_____
		Plus: Additional capital contributions	
		(investments by owner(s) or stock	
		purchases by shareholders)	$_____
		Less: Total deductions (withdrawals	
		by owner(s) or dividends to	
		shareholders)	$_____
		Equality as shown on current	
		Balance Sheet	$_____ ⑫

Source: "Understanding Financial Statements," *Small Business Reporter*, Copyright © Bank of America NT & SA, 1980.

EXHIBIT B1

Sample Blank Balance Sheet

The following text covers the essential elements of a Balance Sheet. Figures used to compile the Balance Sheet are taken from the previous and current Balance Sheet as well as the current **Income Statement** (or **Profit & Loss Statement**). The report is usually attached to the Balance Sheet.

1. **Heading** — The legal name of the business, the type of statement, and the day, month, and year. Must be shown at the top of the report.

2. **Assets** — Anything of value that is owned or legally due the business. Total assets include all **net realizable** and **net book** (also **net carrying**) values. Net realizable and net book values are amounts derived by substracting any estimated allowances for doubtful accounts, depreciation, and reductions of future service — such as amortization of a premium during the term of an insurance policy — from the acquisition price of assets.

3. **Current Assets** — Cash and resources that can be converted into cash within 12 months of the date of the Balance Sheet (or during one established cycle of operations). Besides cash (money on hand and demand deposits in the bank, e.g., checking accounts and regular savings accounts), resources include:

   Accounts Receivable — The amounts due from customers in payment for merchandise or services.

   Inventory — Includes raw materials on hand, work in process, and all finished goods either manufactured or purchased for resale.

   Temporary Investments — Interest- or dividend-yielding holdings expected to be converted into cash within a year. Also called marketable securities or short-term investments, they include stocks and bonds, certificates of deposit, and time deposit savings accounts. List on the Balance Sheet at either their cost or market value, whichever is less.

   Prepaid Expenses — Goods, benefits, or services a business buys or rents in advance of use. Examples are office supplies, insurance protection, and floor space.

4. **Long-Term Investments** — Also called long-term assets. They are holdings the business intends to keep for at least a year and that typically yield interest or dividends. Included are stocks, bonds, and savings accounts earmarked for special purposes.

5. **Fixed Assets** — Fixed assets, frequently called plant and equipment, are the resources a business owns or acquires for use in operations and does not intend for resale. Land is listed at its original purchase price, with no allowance for appreciation or depreciation. Other fixed assets are listed at cost, less depreciation. Fixed assets may be leased. Depending on the leasing arrangement, both the value and the liability of the leased property may need to be listed on the Balance Sheet.

6. **Other Assets** — Resources not listed with any of the above assets. Examples include tangibles such as outdated equipment salable to the scrap yard, and intangibles such as trademarks.

7. **Liabilities** — All monetary obligations of a business and all claims creditors have on its assets.

8. **Current Liabilities** — All debts and obligations payable within 12 months or within one cycle of operations. Typically they are:

   Accounts Payable — Amounts owed to suppliers for goods and services purchased in connection with business operations.

Short-Term Notes — The balance of principal due to pay off short-term debt for borrowed funds.

Current Portion of Long-Term Notes — Current amount due of total balance on notes whose terms exceed 12 months.

Interest Payable — Any accrued fees due for use of both short- and long-term borrowed capital and credit extended to the business.

Taxes Payable — Amounts estimated by an accountant to have been incurred during the accounting period.

Accured Payroll — Salaries and wages currently owned.

9. **Long-Term Liabilities** — Notes, contract payments, or mortgage payments due over a period exceeding 12 months or one cycle of operations. They are listed by outstanding balance, less the current portion due.

10. **Equity** — Also called **net worth.** Equity is the claim of the owner(s) on the assets of the business. In a proprietorship or partnership, equity is each owner's original investment plus any earnings after withdrawals.

    In a corporation, the owners are the shareholders. The corporation's equity is the sum of contributions plus earnings retained after paying dividends.

11. **Total Liabilities and Equity** — The sum of these two amounts must always match that for Total Assets.

12. **Reconcilement of Equity** — Used for proprietorships and partnerships, this report reconciles the equity shown on the current Balance Sheet. It records equity at the beginning of the accounting period and details additions to or subtractions from this amount made during the period. Typically, additions and subtractions are net income or loss and owner contributions and/or deductions.

    For corporations, the same type of report is called the **Statement of Retained Earnings.** It lists increases or decreases in this accumulated net income since the beginning of the current period.

Source: Extracted from "Understanding Financial Statements," *Small Business Reporter*, Copyright © Bank of America NT & SA 1980.

EXHIBIT C

MONTHLY CASH FLOW PROJECTION

	Pre-Start-up Position		1		2-12		TOTAL		
YEAR MONTH							Columns 1–12		
	Estimate	Actual	Estimate	Actual	Estimate	Actual	Estimate	Actual	
1. CASH ON HAND (Beginning of month)									1.
2. CASH RECEIPTS (a) Cash Sales									2. (a)
(b) Collections from Credit Accounts									(b)
(c) Loan or Other Cash injection (Specify)									(c)
3. TOTAL CASH RECEIPTS (2a+2b+2c=3)									3.
4. TOTAL CASH AVAILABLE (Before cash out) (1+3)									4.
5. CASH PAID OUT (a) Purchases (Merchandise)									5. (a)
(b) Gross Wages (Excludes withdrawals)									(b)
(c) Payroll Expenses (Taxes, etc.)									(c)
(d) Outside Services									(d)
(e) Supplies (Office and operating)									(e)
(f) Repairs and Maintenance									(f)
(g) Advertising									(g)
(h) Car, Delivery, and Travel									(h)
(i) Accounting and Legal									(i)
(j) Rent									(j)
(k) Telephone									(k)
(l) Utilities									(l)
(m) Insurance									(m)
(n) Taxes (Real estate, etc.)									(n)
(o) Interest									(o)
(p) Other Expenses (Specify each)									(p)
_____									
_____									
(q) Miscellaneous (Unspecified)									(q)
(r) Subtotal									(r)
(s) Loan Principal Payment									(s)
(t) Capital Purchases (Specify)									(t)
(u) Other Start-up Costs									(u)
(v) Reserve and/or Escrow (Specify)									(v)
(w) Owner's Withdrawal									(w)
6. TOTAL CASH PAID OUT (Total 5a thru 5w)									6.
7. CASH POSITION (End of month) (4 minus 6)									7.
ESSENTIAL OPERATING DATA (Non-cash flow information) A. Sales Volume (Dollars)									A.
B. Accounts Receivable (End of month)									B.
C. Bad Debt (End of month)									C.
D. Inventory on Hand (End of month)									D.
E. Accounts Payable (End of month)									E.
F. Depreciation									F.

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EXHIBIT C1

1. CASH ON HAND (Beginning of month)	Cash on hand same as (7), Cash Position Previous Month
2. CASH RECEIPTS	
(a) Cash Sales	All cash sales. Omit credit sales unless cash is actually received.
(b) Collections from Credit Accounts	Amount to be expected from all credit accounts.
(c) Loan or Other Cash Injection	Indicate here all cash injections not shown in 2(a) or 2(b) above. See "A" of "Analysis"
3. TOTAL CASH RECEIPTS (2a+2b+2c=3)	Self-explanatory
4. TOTAL CASH AVAILABLE (Before cash out) (1+3)	Self-explanatory
5. CASH PAID OUT	
(a) Purchases (Merchandise)	Merchandise for resale or for use in product (paid for in current month)
(b) Gross Wages (Excludes withdrawals)	Base pay plus overtime (if any)
(c) Payroll Expenses (Taxes, etc.)	Include paid vacations, paid sick leave, health insurance, unemployment insurance, etc. (this might be 10 to 45% OF 5(b)
(d) Outside Services	This could include outside labor and/or material for specialized or overflow work, including subcontracting
(e) Supplies (Office and operating)	Items purchased for use in the business (not for resale)
(f) Repairs and Maintenance	Include periodic large expenditures such as painting or decorating
(g) Advertising	This amount should be adequate to maintain sales volume – include telephone book yellow page cost
(h) Car, Delivery, and Travel	If personal car is used, charge in this column – include parking
(i) Accounting and Legal	Outside services, including, for example, bookkeeping
(j) Rent	Real estate only (See 5(p) for other rentals)
(k) Telephone	Self-explanatory
(l) Utilities	Water, heat, light, and/or power
(m) Insurance	Coverages on business property and products e.g. fire, liability; also workman's compensation, fidelity, etc. Exclude "executive" life (include in "5(t)").
(n) Taxes (Real estate, etc.)	Plus inventory tax – sales tax – excise tax, if applicable
(o) Interest	Remember to add interest on loan as it is injected (See 2(c) above)
(p) Other Expenses (Specify each)	Unexpected expenditures may be included here as a safety factor
	Equipment expensed during the month should be included here (Non-capital equipment)
	When equipment is rented or leased, record payments here
(q) Miscellaneous (Unspecified)	Small expenditures for which separate accounts would not be practical
(r) Subtotal	This subtotal indicates cash out for operating costs
(s) Loan Principal Payment	Include payment on all loans, including vehicle and equipment purchases on time payment
(t) Capital Purchases (Specify)	Non-expensed (depreciable) expenditures such as equipment, building, vehicle purchases, and leasehold improvements
(u) Other Start-up Costs	Expenses incurred prior to first month projection and paid for after the "start-up" position
(v) Reserve and/or Escrow (Specify)	Example: Insurance, tax, or equipment escrow to reduce impact of large periodic payments
(w) Owner's Withdrawal	Should include payment for such things as owner's income tax, social security, health insurance, "executive" life insurance premiums, etc.
6. TOTAL CASH PAID OUT (Total 5a thru 5w)	Self-explanatory
7. CASH POSITION (End of month) (4-6)	Enter this amount in (1) Cash on Hand following month – See "A" of "Analysis"
ESSENTIAL OPERATING DATA (Non cash flow information)	This is basic information necessary for proper planning and for proper cash flow projection. In conjunction with this data, the cash flow can be evolved and shown in the above form.
A. Sales Volume (Dollars)	This is a very important figure and should be estimated carefully, taking into account size of facility and employee output as well as realistic anticipated sales (Actual sales performed – not orders received)
B. Accounts Receivable (End of month)	Previous unpaid credit sales plus current month's credit sales, less amounts received current month (deduct "C" below)
C. Bad Debt (End of month)	Bad debts should be subtracted from (B) in the month anticipated
D. Inventory on Hand (End of month)	Last month's inventory plus merchandise received and/or manufactured current month minus amount sold current month
E. Accounts Payable (End of month)	Previous month's payable plus current month's payable minus amount paid during month
F. Depreciation	Established by your accountant, or value of all your equipment divided by useful life (in months) as allowed by Internal Revenue Service

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